CORRIGAN FINANCIAL, INC.

Market Update: December 2023

Global stocks had another strong month with returns of nearly 5% during December. In the fourth quarter alone, domestic and foreign stocks rocketed 12.07% and 9.75%, respectively. Global bond markets also delivered strong returns, advancing 4% in December and 8% for the quarter.

> **Christmas appears to have come early this year, as investors were given much to celebrate this holiday season. Most notably, at the most recent FOMC meeting, Fed Chairman Jerome Powell and his fellow Federal Reserve colleagues "gifted" investors with a "turtle" dovish pivot, sparking a rally in both stocks and bonds.**
>
> **J.P. Morgan Asset Management – Market Insights 12/25/23**

All the major stock indexes closed out the year with nine consecutive weeks of gains. For the S&P 500 Index, that marks the longest streak of weekly gains since January of 2004.

It's interesting to note that global equity values climbed over 14% in just the last two months, after losing 9% during the previous three-month period (August – October). It makes you wonder about the *nervous nellies* or *market-timers* who ran for the exits during the low points of October. At a minimum, it's another example of why investors need to stay disciplined and humble.

Technology stocks saw some of their strongest returns in two decades. The tech-heavy Nasdaq Composite Index, recorded returns of 45% during the calendar year, after being down 33% in 2022. Enthusiasm over the prospects for artificial-intelligence powered the returns of some of the market's biggest companies, most notably the so-called "magnificent seven". While returns over the past couple of months have broadened, still more than two-thirds of the S&P 500 stocks returned less than the overall index in 2023.

> **Startups are racing to build disruptive products and business models, while incumbents are looking to respond. Generative AI has triggered a sense of urgency in enterprises worldwide to develop AI strategies.**
>
> **Jensen Huang, CEO Nvidia – CNBC 12/29/23**

(The 45% return for the Nasdaq Composite sounds great, but for those of us keeping score … tech investors needed to generate a 50% positive return in 2023 just to make up for the 33% decline during 2022. Needless to say, this *downside math* shows how extreme volatility can put a dent in long-term performance measures.)

Investors had their share of hurdles in 2023. For instance, the Fed continued raising rates, the war between Russia and Ukraine entered its second year, some regional banks were caught off-guard by declining bond values, and an attack on Israel by Hamas sparked a war in the Middle East.

Through all that, consumers never stopped spending, inflation continued to decline, and corporate profits started to grow again. To add icing on the cake, investors anticipate the Fed to start cutting rates early in 2024. When it was all said and done, global stock markets provided returns well in excess of 20% to investors in 2023.

> **Almost no one thought 2023 would be a blockbuster year for stocks. They could hardly have been more wrong.**
>
> **Gunjan Banerji – WSJ 12/29/23**

Pretty much everyone expected the U.S. to fall into recession in 2023. Now, the consensus is for a soft landing … meaning that inflation will be tamed, but our economy will continue to prosper. At its December meeting, the Fed held its benchmark fed-funds rate steady, and acknowledged the economic risks of leaving rates too high as inflation falls. Fed officials now anticipate three rate cuts in 2024 … for a dramatic shift in policy.

> **Powell played Santa Claus early. It was a 180-degree shift, right there.**
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> **Diane Swonk, KPMG Chief Economist – WSJ 12/13/23**

The Fed's preferred inflation measure actually declined 0.1% in November from October. That is the first recorded decline since April 2020. For the year, prices were up 2.6%, which is close to the Fed's 2% target. Consumer spending increased 0.2% in November, higher than October's 0.1% advance. Overall personal income increased 0.4% in November, also up slightly from the previous month.

> **While consumers continue to face hurdles from higher borrowing costs, tighter credit conditions and elevated prices, a still-strong labor market, a positive trend in incomes and an easing in price pressures should keep spending and growth positive for now.**
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> **Rubeela Farooqi, High Frequency Economics – WSJ 12/14/23**

The benchmark 10-year U.S. Treasury saw its yield top 5% for the first time in 16 years. Investors took advantage of rising rates by pouring money into money-market funds and bank certificates of deposit.

Bond yields eventually pulled back, and the 10-year Treasury yield settled at 3.86% … ending the year at or around where it started. Remember, bond values rise as yields fall. So, after struggling for most of the year, global bonds ended 2023 delivering returns of close to 6% for investors.

Money-market funds, bank certificates of deposit, and short-term bonds are offering solid yields, but most economists anticipate these yield offerings will diminish during 2024. If short-term rates fall, savers will be forced to reinvest their cash at much lower rates.

> **The threat of reinvestment risk becomes reality in 2024. If the Fed is done with its tightening cycle, investors should lengthen their bonds' maturities. Of course, given the recent volatility in rates, yields could rise from here if inflation perks up. Just like with stocks, getting the timing of this right is really difficult, but beginning to add *duration* does make sense right now.**

Michael Arone, State St. Global Advisors – Barron's 12/21/23

After five months of declines, housing sales increased 0.8% in November from the previous month, according to the National Association of Realtors (NAR). November sales remain 7.3% lower year-over-year, and existing-home sales should end the year at the lowest level since 2011.

In October, home affordability fell to its worst level in almost 40 years. With interest rates recently declining below 7%, affordability measures are getting some needed relief. Still, inventory measures remain at historical lows, while home prices remain at historical highs. The NAR reported the national median existing-home price was $367,600 in November … 4% higher than a year earlier.

> **Even though mortgage rates have come down, however, they would probably need to decline much more to substantially unlock the market for previously owned, or existing, homes. The lock-in effect, where homeowners are unwilling to sell and give up the much lower mortgage rates they are paying, persists … That is good news for home builders.**

Justin Lahart – WSJ 12/20/23

Goldman Sachs economists estimate that core inflation across the globe – measured against the economies that experienced the post-Covid inflation surge – ran at an annualized pace of 2.2% over the three months ended November. They anticipate that inflation will be at or near inflation targets by the end of 2024. Bank of America strategists project 152 global central bank rate cuts next year, the most since 2009.

> **Call it a Christmas miracle: Inflation around the globe is slowing way faster than expected. If economists are right, the gift will keep on giving next year, bringing inflation back to normal levels for the first time in three years.**

Gwynn Guilford – WSJ 12/24/23

Economic growth across the globe was uneven at best. The U.S. defied predictions of recession and turned in solid growth. Europe avoided recession, but its economy was basically flat for the year. China's economy continues to struggle, as the property bust feeds into overall consumer confidence.

In December, Moody's Investors Service lowered its outlook for China's credit rating from stable to negative. Moody's kept its long-term rating of A1 on the nation's sovereign debt (four levels below its Aaa rating).

> **The outlook change signaled how the risks from China's local government debts have become too big to ignore.**

Weilun Soon – WSJ 12/5/23

It is now estimated that China's off-balance sheet debt (so-called hidden-debt) has ballooned to close to $11 trillion. The actual number remains unknown, but the debt levels are considered to be unsustainable.

> **For more than a decade, Chinese regulators have been trying to address the risks of the country's hidden debt … China is trying to defuse a financial time bomb that could severely damage its banking system.**

Feng/Li – WSJ 12/5/23

In baseball terms, it looks like the inflation battle is in at least the 8^{th} or maybe even in the 9^{th} inning. Recession concerns are in the rearview mirror, rate cuts are on the way, and we are destined to stick a soft-landing. What could go wrong?

Yes, Wall Street appears to be quite optimistic for the new year. That sounds great, but just how has the "consensus" done over the past few years? At the end of 2020, investors were still in love with the popular pandemic-related stocks, at the end of 2021 they were confident that tech stocks would continue their climb, and at the end of 2022 they were certain we were on the brink of recession.

> **This December, they believe, again with absolute conviction, that the economy is heading for a soft landing and lower interest rates. Maybe this time they will be right.**
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> **Then again, maybe not. Being in the crowd is always an uncomfortable place for an investor, but agreeing with such a strong consensus is especially difficult, because if it turns out wrong, the punishment from the markets will be painful – just as it was in each of the past three years.**
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> **James Mackintosh – WSJ 12/15/23**

According to the International Monetary Fund, the U.S. government is running deficits at all levels of government that combined are more than 8% of GDP. That is way above last year's 3.7% deficit measure and much higher than any other developed country.

You may have heard that total U.S. federal debt just reached $34 trillion. Also, let's not forget the near-term funding concerns facing U.S. entitlement programs … concerns that need to be resolved sooner rather than later. Needless to say, our escalating U.S. national debt is a big problem that is staring us right in the face.

> **In the future, when investors debate risks and investment strategies, 2023 is destined to be cited as a case study when seemingly insurmountable risks succumbed to significant gains.**
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> **Risk doesn't exist – until it does. When that happens, the undisciplined and overconfident will feel like tourists who have returned from a great trip, only to get into a bad accident on their way back from the airport.**
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> **Steven M. Sears – Barron's 12/27/23**

To be sure, we will remain disciplined and humble. I hope you all have a happy and healthy 2024!

Daniel G. Corrigan, CPA/PFS, CFP ®